**UNITED STATES DISTRICT COURT**

**DISTRICT OF CONNECTICUT**

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| TIG INSURANCE COMPANY, | : | |
| Petitioner, | : | |
| | : | |
| -vs- | : | Civil No. 3:02cv2206 (PCD) |
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| SECURITY INSURANCE COMPANY OF HARTFORD, | : | |
| Respondent. | : | |

RULINGS ON MOTION TO CONFIRM INTERIM ARBITRATION AWARD AND MOTION TO VACATE INTERIM ARBITRATION AWARD

Petitioner moves to confirm an interim arbitration award pursuant to the Federal Arbitration Act, 9 U.S.C. § 1, *et seq*. Respondent moves to vacate the interim arbitration award. For the reasons set forth herein, petitioner's motion to confirm the arbitration award is **denied** and respondent's motion to vacate the arbitration award is **granted**.

I. BACKGROUND

Petitioner and respondent entered into a Workers Compensation Underlying First, Second and Third Excess of Loss Reinsurance Agreement ("Reinsurance Agreement"), effective January 1, 1999. The Reinsurance Agreement contains a clause requiring arbitration of all disputes.[1] By letter dated April 29, 2002, respondent notified petitioner that further claim

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[1]The arbitration clause provides as follows:

As a condition to any right of action hereunder, any irreconcilable dispute between the parties to this Agreement shall be submitted to a board of arbitration composed of two arbitrators and an umpire meeting at a place to be agreed by the board.

Arbitration shall be initiated by the delivery of a written notice of demand for arbitration by one party to the other within a reasonable time after the dispute has arisen.

The members of the board of arbitration shall be active or retired, disinterested officials of insurance or reinsurance companies, or underwriters at Lloyd's, London, not under the control or management of either party to this Agreement. Each party shall appoint its arbitrator, and two

payments under the Reinsurance Agreement were suspended pending an investigation into potential grounds for rescinding the same. By letter dated June 27, 2002, petitioner notified respondent of its intention to refer the matter to arbitration. Through arbitration, it sought an award:

> (1) declaring the [Reinsurance Agreement] to be valid and enforceable; (2) finding that the [Reinsurance Agreement] was not induced by fraud or negligent representation as alleged by Trustmark Insurance Company ("Trustmark"); (3) ordering [respondent] to pay all outstanding balances, together with interest, costs and attorneys' fees; and (4) granting [petitioner] any further relief that the Panel deems appropriate. [Petitioner] will also ask the Panel to issue an interim award requiring [respondent] to post collateral pending the outcome of the arbitration in an amount sufficient to secure [respondent's] obligations under the [Reinsurance Agreement].

The three-member panel was appointed, at which time the parties submitted their statements of

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arbitrators shall choose an umpire before instituting the hearing. If the respondent fails to appoint its arbitrator within four weeks after being requested to do so by the claimant, the latter shall also appoint the second arbitrator. If the two arbitrators fail to agree upon the appointment of the umpire within four weeks after their nominations, each of them shall name three of whom the other shall decline two, and the decision shall be made by drawing lots. The claimant shall submit its brief within 45 days from appointment of the umpire. The respondent shall submit its brief within 45 days thereafter, and the claimant may submit a reply brief within 30 days after filing of the respondent's brief.

The board shall make its decision with regard to the custom and usage of the insurance and reinsurance business. The board shall issue its decision in writing based upon a hearing in which evidence may be introduced without following strict rules of evidence but in which cross-examination and rebuttal shall be allowed. The board shall make its decision within 60 days following the termination of the hearings unless the parties consent to an extension. The majority decision of the board shall be final and binding upon all parties to the proceeding. Judgment may be entered upon the award of the board in any court having jurisdiction.

Each party shall bear the expense of its own arbitrator and shall jointly and equally bear with the other party the expense of the umpire. The remaining costs of the arbitration proceedings shall be allocated by the board.

The majority decision of the board shall be final and binding upon all parties to the proceeding. Judgment may be entered upon the award of the board in any court having jurisdiction.

Article XVII, Reinsurance Agreement.

position.

> In its statement of issues dated November 19, 2002, petitioner sought an award:
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> > (I) ordering [respondent] to pay all outstanding balances currently due under the [Reinsurance Agreement] ($38,934,695 as of October 31, 2002), plus interest, costs and attorneys' fees, (ii) further ordering [respondent] to pay in accordance with the terms of the [Reinsurance Agreement] all future amounts as they become due, and (iii) granting such other relief as the Panel deems appropriate.

In its statement of position, respondent indicated that Trustmark, a party not involved in the arbitration, initially raised claims of fraud against petitioner in district court actions involving a separate retrocession agreement. Respondent alleged that it attempted to investigate the allegation but petitioner rather than providing requested information instead commenced arbitration proceedings. Respondent therefore took the position that Trustmark's allegation, if substantiated, would provide grounds for rescission but it needed an opportunity to investigate the allegations, requesting discovery until April 7, 2003 and briefing by June 7, 2003. It further took the position that the panel lacked authority to order respondent to post a bond for breach of an agreement that may be rescinded and asked that such a request be decided through formal motion.

On November 25, 2002, the parties met for what was described as an organizational meeting. During the meeting, the panel heard argument from the parties and recessed. After the recess, Umpire Franklin Haftl stated:

> As you can imagine, the panel had considerable deliberation on this serious matter. The first issue is that [petitioner] should advise by Wednesday to [respondent] the amount of paid losses that are due through October 2002. I assume there will be no disagreement on those figures. If there is, you would

> have to come immediately to the panel. But it is around $38 million. The panel must ask, then, that [respondent] pay that $38 million within ten days of the 27th.

11/25/02 Hearing Tr. at 47-48. Umpire Haftl further ordered a schedule of discovery and briefing consistent with respondent's statement of issues. Respondent objected to the panel's order when issued.

By letter dated November 26, 2002, petitioner clarified the characterization and amount as follows: $31,978,197.38 in paid loss balances and $6,247,795.00 in premium receivables. The amounts were detailed as follows: total premiums paid to respondent: $71,900,469.96; total losses billed to respondent: $56,971,236.95; total losses paid by respondent: $24,993,039.57; and total outstanding losses: $31,978,197.38. Respondent disagreed as to these amounts and proposed alternative figures. On December 9, 2002, respondent notified petitioner via e-mail that it believed the order of the panel to be unenforceable and would therefore not comply with its terms. On December 11, 2002, the Panel clarified its November 25, 2002 order as requiring respondent to pay petitioner all outstanding balances due under the Reinsurance Agreement as of October 31, 2002, including paid losses and premiums receivable, totaling $38,152,252.37, by December 16, 2002. Petitioner then filed the present action to confirm the interim award.

II. DISCUSSION

Respondent moves to vacate the interim arbitration award arguing that the award does not constitute a final award subject to confirmation by this Court. Petitioner responds that the

award should be confirmed as it is final as to a separate independent claim.[2]

An arbitration award is final for purposes of the FAA when "intended by the arbitrators to be their complete determination of all claims submitted to them." *Michaels v. Mariforum Shipping, S.A.*, 624 F.2d 411, 413 (2d Cir. 1980). A claim is completely determined when both the question of liability and of damages are decided. *See id.* at 414. A court has no authority to review an award lacking the requisite degree of finality. *See id.*, and such an award shall be vacated pursuant to 9 U.S.C. § 10(a)(4), *see Michaels*, 624 F.2d at 414.

This general requirement is subject to certain exceptions. *See Hart Surgical, Inc. v. Ultracision, Inc.*, 244 F.3d 231, 233 (1st Cir. 2001). An interlocutory award is subject to confirmation if it involves a separate and independent claim, *see Metallgesellschaft A.G. v. M/V Capitan Constante*, 790 F.2d 280, 283 (2d Cir.1986); *Sperry Int'l Trade v. Israel*, 689 F.2d 301, 304 n.3 (2d Cir.1982). Petitioner argues that the present award is the result of such a separate and independent claim.

In its letter, petitioner sought an award "ordering Security to pay all outstanding balances" under the Reinsurance Agreement. It argues that the panel's award separately and definitively resolves the issue of respondent's obligation to make payments under the Reinsurance Agreement, an issue wholly unrelated to whether the Reinsurance Agreement is ultimately rescinded. Respondent disagrees with this proposition, arguing the issues involved are dependent and do not lend themselves to separate resolution.

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[2] This Court does not reach the issues of whether the award issued in violation of respondent's right to fundamental fairness and whether the Panel lacked authority to issue the award.

Petitioner's argument stands or falls on the applicability of the exception set forth in *Metallgesellschaft A.G.* As such a brief discussion of the issues involved therein is helpful. The dispute in *Metallgesellschaft A.G.* involved compliance with a charter agreement by which the registered owner of the Capitan Constante agreed to ship approximately 53,000 metric tons of fuel oil from Argentina to New York. *See Metallgesellschaft A.G.*, 790 F.2d at 280. The vessel delivered the fuel to New York and invoiced Metallgesellschaft for the delivery. *See id.* at 281. Rather than paying the invoice, on the day prior to completion of the fuel offload Metallgesellschaft filed a complaint in federal district court alleging short delivery and contaminated fuel, which was met by a counterclaim for freight earned, demurrage, and dead freight. *See id.* The vessel owner then invoked his right to arbitrate provided in the charter. *See id.*

Although Metallgesellschaft's claims were unresolved at the time, the arbitration panel found "no dispute as to the amount of freight which [the shipowner] had earned and that, by clear and unambiguous language, the parties expressly dealt with the payment of freight in a special manner." *Id.* (internal quotation marks omitted). The district court confirmed the interim award, concluding that "the demand for freight was a separate, independent claim, not subject to any offset, and, being wholly independent of other issues, could be finally disposed of separately." *Id.* The judgment was affirmed on appeal based on the provision in the charter adopting ancient maritime law requiring that "where freight is payable on delivery, it should be paid concurrently with the delivery of the goods." *Id.* The ancient law, existing prior to rights of set-off and counterclaim, accommodated the "hand to mouth" operation of some shipowners

whose business could not financially withstand protracted litigation to recover freight cost. *See id.* The charter provision involved, which required that "freight shall be computed on intake quantity and shall be payable without discount on delivery," *id.* at 282, was found to embrace the ancient law by agreement and thus required immediate payment for goods delivered regardless of opposing parties right to "set-off, recoupment, abatement, defalcation, or counterclaim." *Id.*

A number of considerations are evident in the decision affirming the interim award. First, the interim award was consistent with "the clearly expressed intent of the parties." *Id.* Second, the beneficiary of the interim award "undoubtedly would have been entitled to summary judgment in its favor for the amount of the unpaid freight," *id.*, as precedent dictated that the counterclaims were "'legally irrelevant' to the question of the owner's claim for freight," *id.*, and thus constituted an "independent obligation payable regardless of any [other] claims," *id.* Third, as the shipowner would legally be entitled to damages in a court action without action on the remaining claims, a decision denying the same "the same prompt and commercially important relief," *id.*, would be absurd given the goal of arbitration to render prompt and inexpensive dispute resolution, *see id.*

In the present case, petitioner appears to argue that the parties clearly intended and contemplated such an interim award by virtue of respondent's failure to object to its letter invoking the arbitration clause. Petitioner, however, points to no legal authority by which respondent, in failure to object to the letter, would be considered to have clearly intended and in fact agreed to such an award. In general, conduct or silence in response to such a notice

would not ordinarily be considered acceptance unless, under the circumstances, a response reasonably would be anticipated on receipt of such notice. *The Cutchogue*, 10 F.2d 671, 673 (2d Cir. 1926); *see also C. L. Wold v. League of the Cross of the Archdiocese of San Francisco, Inc.*, 114 Cal. App. 474, 479; 300 P. 57, 60 (1926)[3] ("[o]rdinarily mere silence or inaction in the face of the offer of a contract cannot amount to an acceptance. The circumstances must be such as to impose upon the offeree a duty to speak if he is to be held bound to a contract by remaining mute."). Petitioner provides no support for this novel proposition imposing an obligation on respondent to object on peril of agreement, and it further appears that respondent did in fact disagree in both its statement of issues and at the organizational meeting to the panel's so doing. The Reinsurance Agreement, unlike the charter in *Metallgesellschaft A.G.*, does not expressly provide procedurally for such an award, nor does the agreement implicate traditions or policy in the insurance industry substantiating a legal basis for such an award.

Nor can an order rescinding a contract be characterized as legally irrelevant to an obligation to pay pursuant to the terms of the contract. Rescission extinguishes one's obligations under a contract. *See* CAL. CIV. CODE § 1688. If the Reinsurance Agreement is found to have been rescinded, then there necessarily is no obligation to pay pursuant to the same. The issues of rescission and obligation to pay therefore are dependent, the resolution of

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3 The Reinsurance Agreement provides in Article XVIII that it is to be governed by California law, and as such the parties are presumed not to have elected to apply other law. If such were the case, the principles involved herein are consistent with general contract law and would likely be unaffected by choice of law.

the former affecting awards of damages for the latter. The distinction is as fundamental as the order of damages to which petitioner would be entitled. If the agreement is found to be rescinded, petitioner will receive damages in the form of restitution for premiums paid, *see* CAL. CIV. CODE § 1692; if the agreement is breached, the order of damages will be its expectation interest, *see* CAL. CIV. CODE § 3300. Further, nothing in the present case supports a theory that an award may issue irrespective of a right or set-off or counterclaim, which rights the panel has granted respondent a period of discovery to investigate properly.

Finally, a refusal to characterize the present interim award as final does not offend the goals of arbitration. In *Metallgesellschaft A.G.*, the express provisions of the charter adopted ancient maritime law requiring payment on delivery irrespective of counterclaims. Such provision required immediate payment of the debt, and as the charter provisions were boilerplate at the time, neither party could claim surprise at the result. No express agreement requiring immediate satisfaction is at work in the present case, and respondent in fact objected twice to petitioner's claim for an early award in the form of a prejudgment remedy. Although petitioner may have asked for an immediate remedy, such remedy, as evident in *Metallgesellschaft A.G.*, is only appropriate when a court would be required to issue the same. Such is not the case with the contract issues involved herein. It cannot be said that the result is inconsistent with the result that would be anticipated from a court.

In an effort to resolve these discrepancies, petitioner cites *Island Creek Coal Sales Co. v. Gainesville*, 729 F.2d 1046 (6th Cir. 1984). In *Gainesville*, the City of Gainesville entered into an agreement to buy coal. *Id.* at 1047. The price of coal declined and the City

sought to terminate the agreement alleging that Island Creek Coal Sales Company had illegally assigned the contract. *Id.* Through arbitration, it sought declarations that Island Creek had breached the agreement and that the City had a right to terminate the agreement. *Id.* After the proceedings had concluded but prior to the issuance of an award, the City announced its intention to terminate the contract. *Id.* at 1048. The parties conferred with the panel, after which the panel ordered the City to continue receiving shipments of coal as per the agreement and issued an interim order to that effect. The interim order was confirmed. *See id.* The Sixth Circuit Court of Appeals affirmed holding that the panel had the authority under its "power to prevent" to order specific performance, *see id.* at 1049, and that the issue of whether the City was required to perform under the agreement *during the pendency of the arbitration proceedings* was separate and independent, *see id*.

Petitioner's argument that *Island Creek* is directly on point and thus requires respondent "to perform the contract by paying outside balances during the pendency of the arbitration" misses the mark. As an initial matter, the interim award in *Island Creek* constituted a response to an issue that arose during the course of arbitration and was dealt with through an order maintaining the status quo. The consistent theme throughout the cases cited by petitioner is the order constituted a form of prejudgment remedy that would be expected in any district court. Such is not the case with an order to pay an amount in damages. The order to pay $38 million substantially changes the position of the parties from the outset of arbitration and deprives respondent of possession of the funds. It is thus not a status quo arrangement requiring continued payments under an agreement that were made at the outset of arbitration as

in *Island Creek* but rather a partial resolution of a number of issue submitted to arbitration. As such, the order lacks the requisite finality requiring an order from this Court vacating the same.

III. CONCLUSION

Petitioner's motion to confirm the arbitration award (Doc. No. 4) is **denied**. Respondent's motion to vacate the arbitration award (Doc. No. 13) is **granted**. The Clerk shall close the file.

SO ORDERED.

Dated at New Haven, Connecticut, January ___, 2003.

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Peter C. Dorsey
United States District Judge